

FILED

MAR 31 2015

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA
SACRAMENTO DIVISION

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

KMS

In re

Case No. 10-31713-A-7

WILLIAM ROBERT ESHELMAN,

Debtor.

PAUL BENSI, ET AL.,

Adv. No. 10-2473
[Consolidated with 10-2476]

Plaintiff,

vs.

WILLIAM ROBERT ESHELMAN,

Defendant.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This proceeding concerns the dischargeability of a debt allegedly owed by defendant and debtor William Roger Eshelman to plaintiffs Stationary Engineers Local 39 Pension Trust Fund, Stationary Engineers Local 39 Annuity Trust Fund, and Stationary Engineers Local 39 Health and Welfare Trust Fund ("Trust Funds"), and Stationary Engineers Local 39 International Union of Operating Engineers AFL-CIO ("Engineers Union").

1 The alleged debt arises from unpaid employer contributions
2 and a withdrawal liability in connection with AC Service & Design
3 Company's (ACSD) participation as an employer in the Trust Funds.
4 See Employee Retirement Income Security Act (ERISA) of 1974 (Pub.
5 L. No. 93-406, codified at 29 U.S.C. §§ 1002 et seq.).
6 Plaintiffs challenge Eshelman's right to discharge this debt
7 under 11 U.S.C. § 523(a)(4) and (6).

8 Jurisdiction exists under 28 U.S.C. § 1334. Venue is proper
9 under 28 U.S.C. § 1409. The District Court for the Eastern
10 District of California has referred bankruptcy cases and
11 proceedings to the Bankruptcy Court for hearing pursuant to 28
12 U.S.C. § 157(a) and United States District Court, Eastern
13 District of California General Orders 182 and 223. This is a
14 core proceeding. 28 U.S.C. § 157(b)(2)(I).

15 After dismissal of the First Claim for Relief and all fraud
16 allegations in the Second Claim for Relief, the remaining claims
17 in the Second Amended Complaint are for defalcation by a
18 fiduciary, and damages for willful and malicious injury to the
19 plaintiffs' property.

20 21 Findings of Fact

22 1. Eshelman opened ACSD in 1988 as a sole-proprietorship
23 and incorporated it in 1995. ACSD was a family business that
24 employed Eshelman's wife Kathy Eshelman, their son and
25 daughter-in-law. Eshelman was the President and sole shareholder
26 of ACSD. He was involved in the day to day operations of the
27 business and his general responsibilities included working at job
28 sites, sales, marketing, customer relations, hiring and training

1 field employees, record keeping, and other management related
2 duties. Eshelman worked at ACSD full time.

3 2. ACSD initially hired plumbers, service mechanics, and
4 sheet metal workers doing new construction, remodeling of
5 commercial buildings, and maintenance, service and repair, with
6 skills specific to the air conditioning industry. ACSD employed
7 between two and twenty people at various times.

8 3. On or about June 30, 1990, Eshelman opened AC Service,
9 Inc., as a California corporation and transferred the ACSD sheet
10 metal operations into AC Service, Inc. AC Service, Inc., was
11 sold in 1992.

12 4. Mrs. Eshelman began working for ACSD part-time in 1990,
13 and became a full-time employee in 1992. Mrs. Eshelman was the
14 operations manager at ACSD. Her duties included accounting,
15 payroll, personnel matters, supervising the office manager, and
16 completing monthly reports for the unions after ACSD became a
17 union shop. Once Mrs. Eshelman became a full-time employee at
18 ACSD, Eshelman's job duties were changed to sales, estimating,
19 customer relations and supervising jobs.

20 5. ACSD was a non-union company until about 1992, when it
21 signed a collective bargaining agreement ("CBA") with the
22 Engineers Union.

23 6. At the same time, ACSD signed a "Letter of
24 Understanding" that allowed ACSD employees who were not members
25 of the Engineers Union to participate in the Engineers' Union
26 health plan through the Health and Welfare Trust Fund. Eshelman
27 was told, however, that Eshelman was not entitled to health
28 benefits because Eshelman was considered the owner or employer.

1 7. Each of the respective Trust Funds is governed by a
2 Trust Agreement that requires the employer to make contributions
3 to the Trust Funds and governs the employer's responsibilities to
4 the Trust Funds. When an employer such as ACSD becomes signatory
5 to the CBA, the employer is bound by the language of those
6 agreements to the Trust Fund Agreements applicable to that
7 employer.

8 8. Eshelman did not recall ever seeing a copy of any of
9 the Trust Fund Agreements at any time prior to April 2, 2008,
10 when the Trust Funds sued ACSD in the U.S. District Court for the
11 Northern District of California for \$136,132.72 plus interest and
12 attorneys' fees. Eshelman was not named as a defendant in the
13 district court case.

14 9. Nobody from the Engineers Union or the Trust Funds ever
15 discussed or explained the Trust Fund Agreements to Eshelman.
16 The Trust Fund Agreements were not attached to or included with
17 any of the CBAs that Eshelman signed.

18 10. ACSD periodically renewed the CBAs from 1992 to 2008.
19 ACSD also signed CBAs with the Plumbers Union as well as the
20 Local 104 of the Sheet Metal Workers Union. As customer jobs
21 would come up, Eshelman would assign the employee most qualified
22 based on his particular skill set, regardless of union
23 affiliation. Eshelman believed he was permitted to make this
24 selection under the CBA. For example, one CBA effective from
25 November 1, 2004, to October 31, 2008, provided: "Employer has
26 the sole right to determine which of the employees (regardless of
27 Union affiliation) shall be assigned or dispatched to specific
28 service work."

1 11. Coverage under the Health & Welfare Fund consists of
2 full coverage for the employee, spouse, and all eligible
3 dependents.

4 12. When Mrs. Eshelman became a full time employee at ACSD,
5 she signed up for health benefits from the Engineers Union, and
6 added Eshelman as her dependent. The Engineers Union was
7 notified of this as part of the ACSD ordinary business practice.
8 Throughout the period covered by the CBAs, ACSD prepared and
9 submitted timely monthly reports to the Engineers Union regarding
10 contributions for employee benefits to the Trust Funds. Mrs.
11 Eshelman completed and submitted these monthly reports to the
12 Engineers Union starting in about 1992.

13 13. Since signing the CBAs, auditors from the Engineers
14 Union and Trust Funds have had full and unfettered access to all
15 ACSD records, and conducted detailed and extensive audits of ACSD
16 records including all payroll records. These audits were done
17 every three to four years. Eshelman was present during these
18 audits, which usually lasted a few days. Eshelman made sure the
19 auditors had access to all ACSD records they requested.

20 14. Compliance Audit Services ("CAS") conducted an audit of
21 ACSD's contributions to the Trust Funds in 2003 ("1999 - 2002
22 Audit").

23 15. Eshelman received a letter, dated March 25, 2003, from
24 the Engineers Union, stating that as a result of the 1999 - 2002
25 Audit, ACSD owed approximately \$2,543.70 for the employee
26 liability of Allen Welch. Eshelman took comfort from this letter
27 that ACSD was properly reporting and in compliance with its
28 obligations under the CBA and various Trust Fund Agreements and

1 Amendments.

2 16. On April 13, 2003, Eshelman received a second letter
3 from the Local 39 again demanding the \$2,543.70, with accrued
4 interest and costs. No demand was made for amounts due and owing
5 for contributions not paid on behalf of Eshelman or Mrs.
6 Eshelman.

7 17. The amount owed from the 1999-2002 audit was paid in
8 full by ACSD.

9 18. Eshelman retired from his full-time employment at ACSD
10 in 2003 due to health reasons. Thereafter his job duties were
11 limited to working from a home office, handling customer
12 relations, and estimating sales.

13 19. On February 4, 2004, Mrs. Eshelman submitted a change
14 of address form to the Engineers Union. Eshelman again was
15 listed as Mrs. Eshelman's dependent.

16 20. In July, 2006 ACSD hired Jim Geist as a salaried
17 salesperson.

18 21. Shortly after ACSD hired Geist, his spouse became ill
19 with a serious medical condition. Eshelman had no knowledge
20 Geist's spouse was ill at the time ACSD hired Geist.

21 22. Eshelman called the Trust Funds to find out about the
22 Geists' medical coverage. During this call, Eshelman was told
23 that ACSD had to fire Geist. Eshelman refused to fire Geist. In
24 response, the Trust Fund representative threatened to "come down
25 there and take [Eshelman] out."

26 23. On or about September 13, 2006, the Trust Fund arranged
27 for Kyle S. Whittemore of Lindquist LLP to audit of ACSD.

28 24. ACSD received a letter dated September 15, 2006,

1 informing it that another audit would be conducted by Lindquist
2 to determine what, if any, contributions were owed to the Trust
3 Funds from 2003 - 2006.

4 25. On October 3, 2006, ACSD received a second notification
5 from Lindquist LLP that the scope of the audit had been expanded
6 to cover 1999 - 2006 (the "2006 audit"). ACSD received no
7 explanation from the Engineers Union or Trust Funds as to why a
8 second audit covering the 1999 - 2002 time period was conducted
9 and/or required.

10 26. In early 2007 ACSD was notified by the Trust Funds the
11 2006 Audit revealed that ACSD owed \$136,132.72.

12 27. Eshelman wrote to the Trust Funds on April 10, 2007,
13 disputing the audit findings. The reference in the 2006 Audit
14 Report to the "probation" issue concerns ACSD's employment policy
15 of not offering fringe benefits to new hires during a 90-day
16 initial probationary period. Eshelman believed that was
17 appropriate under the CBA and was advised by a representative of
18 the Engineers Union that this practice was acceptable.

19 28. In late 2007, the Trust Funds amended the Trust
20 Agreements to add the following language:

21 A. Effective October 1, 2007, Article I, Section 11 is
22 amended as follows:

23 1.08. The term "Contribution" means any contribution
24 made or to be made to the Fund by an Individual
25 Employer under the provisions of the Collective
26 Bargaining Agreement. All contributions, including
27 unpaid contributions, are vested assets of the Trust
28 Fund that vest prior to actual transfer from Employer
to the Fund.

29. Prior to the Amendment effective October 1, 2007, the
Trust Agreements contained the following language with respect to

1 "Contributions":

2 The term "Contribution" means any contribution made or
3 to be made to the fund by an Individual Employer under
the provisions of a Collective Bargaining Agreement.

4 30. On February 6, 2008, ACSD received a letter from the
5 Trust Funds' attorneys demanding payment of the \$136,132.72
6 within 15 business days or a lawsuit would be filed. When
7 payment was not made, the district court case was filed on April
8 2, 2008. Eshelman was not a defendant in the district court
9 case.

10 31. In the district court case, the Trust Funds obtained an
11 order in connection with motions for summary judgment on February
12 4, 2009, determining that ACSD owed unpaid contributions totaling
13 \$34,755.55, comprised of \$10,012.97 to the Health & Welfare Fund,
14 \$7,508.75 to the Pension Fund, \$3,354.60 to the Annuity Fund, and
15 another underpayment of \$13,879.18. However, a judgment was not
16 entered.

17 32. ACSD filed a Chapter 7 bankruptcy on March 30, 2009 in
18 the San Jose Division of the U.S. Bankruptcy Court for the
19 Northern District of California, Case No. 09-52254.

20 33. Neither the ACSD board of directors nor Eshelman were
21 named fiduciaries of the Trust Funds.

22 34. Neither the ACSD board of directors nor Eshelman had
23 any authority over the assets of the Trust Funds, nor is there
24 evidence they were designated to act for named fiduciaries of the
25 Trust Funds.

26 35. Even though the district court determined that only
27 \$34,755.55 of the \$136,132.72 demanded against ACSD was owed, the
28 plaintiffs again seek \$136,132.72, plus interest, auditor's fees,

1 costs, and attorney's fees from Eshelman. With these additional
2 charges, the demand has increased to \$164,859.97.

3 36. However, the plaintiffs failed to substantiate this or
4 any other amount was due. The only evidence offered was the 2006
5 audit report. That is, the court was given the conclusion of the
6 auditors but no attempt was made to lay out the data from which
7 the auditor's conclusion was drawn. This is evidence only that
8 an audit was performed. The court must come to its own
9 conclusions regarding the existence of a liability. This
10 required the data behind audit findings, which was not produced.
11 And, to the extent the audit is probative, considering the
12 context in which the audit was performed, it carries no
13 credibility.

14 37. The Trust Funds also seek payment of an ERISA
15 withdrawal liability. This represents a share of unfunded vested
16 benefits in connection with a multi-employer benefit plan. No
17 convincing evidence was offered by the plaintiffs regarding this
18 liability and how it should be calculated.

19
20 Conclusions of Law

21 1. Assuming the plaintiffs are owed the debts demanded in
22 the second amended complaint, the court concludes they are
23 dischargeable.

24 2. While the failure to make employer contributions and
25 pay a withdrawal liability may be breaches of the Trust Fund
26 Agreements, even an intentional breach of contract is a
27 dischargeable obligation in bankruptcy. See Lockerby v. Sierra,
28 535 F.3d 1038 (9th Cir. 2008) and Petralia v. Jercich (In re

1 Jercich), 238 F.3d 1202, 1205 (9th Cir. 2001). In order for an
2 obligation to be nondischargeable under 11 U.S.C. § 523(a)(6),
3 the debtor must have committed "tortious" conduct.

4 3. The closest the plaintiffs come to establishing
5 tortious, i.e., willful and malicious, conduct by Eshelman, is
6 the failure to make contributions for his own benefits and his
7 receipt of benefits as a dependent of his spouse.

8 4. Section 523(a)(6) requires a "malicious injury." This
9 requires "(1) a wrongful act, (2) done intentionally, (3) which
10 necessarily causes injury, and (4) is done without just cause or
11 excuse." Jercich, 238 F.3d at 1209). Here, Eshelman was told he
12 was not entitled to benefits in his own right and when he
13 received benefits through his spouse after she became a full-time
14 employee of ACSD, this was reported regularly to the Trust Funds
15 and was not challenged in the 1999 - 2002 Audit. The court
16 cannot conclude that Eshelman contrived a scheme to obtain
17 benefits without paying for them in knowing violation of the
18 terms of the Trust Agreements, or that he attempted to conceal
19 the fact that he was receiving benefits without paying for them.

20 5. The plaintiffs also maintain that the ACSD and Eshelman
21 are responsible for unpaid employer contributions in connection
22 with work done by employees who were not members of the unions
23 covered by the plaintiffs' CBAs. Assuming this is so, once again
24 this may be a breach of the Trust Agreements but it is not
25 tortious conduct. The court is unconvinced that Eshelman even
26 understood the agreements to require these payments and then
27 failed to make them.

28 6. Finally, this is not a case in which an employer has

1 withheld money from employees for transmittal to the employees'
2 unions and then failed to remit those funds. The contributions
3 in question were owed by ACSD to the Trust Funds.

4 7. The plaintiffs' primary claim is that the alleged debt
5 is made nondischargeable by 11 U.S.C. § 523(a)(4). That is, they
6 maintain that Eshelman cannot discharge the debt because it
7 arises from a "defalcation while acting in a fiduciary
8 capacity. . . ."

9 8. Whether a person is a fiduciary under section 523(a)(4)
10 is a question of federal law. See Ragsdale v. Haller (In re
11 Haller), 780 F.2d 794, 795 (9th Cir. 1986). In this circuit, an
12 ERISA fiduciary is a fiduciary for purposes of section 523(a)(4).
13 See Blyler v. Hemmeter (In re Hemmeter), 242 F.3d 1186, 1190 (9th
14 Cir. 2001).

15 9. As found above, Eshelman was neither named as a
16 fiduciary nor was the ACSD board of director named as a fiduciary
17 of the Trust Funds. Further, they were not designated to act for
18 named fiduciaries of the Trust Funds.

19 10. Despite these findings, it is still possible that
20 Eshelman could be an ERISA fiduciary if he exercised any control
21 over the assets of the benefit plans. A person is a fiduciary
22 for purposes of ERISA "to the extent (i) he exercises any
23 authority or control respecting management or disposition of its
24 assets. . . ." 29 U.S.C. § 1002(21)(A).

25 11. The plaintiffs argue that Eshelman was a fiduciary
26 under ERISA because he exercised control over a plan asset - the
27 unpaid but owing employer contributions and the unpaid withdrawal
28 liability. His failure to cause ACSD to pay these liabilities

1 therefore was a defalcation by a fiduciary within the meaning of
2 section 523(a)(4).

3 12. The Ninth Circuit, however, has concluded that plan
4 assets of an ERISA trust do not include future contributions.
5 See Collins v. Pension & Ins. Comm. the S. Cal. Rock Prods. &
6 Ready Mixed Concrete Assns., 144 F.3d 1279, 1282 (9th Cir. 1998),
7 and Cline v. Industrial Maintenance Eng. & Contr. Co., 200 F.3d
8 1223 (9th Cir. 2000). So, even if Eshelman was a fiduciary the
9 failure to pay the contributions and withdrawal liability
10 arguably was not a defalcation.

11 13. On the other hand, as noted in findings 28 and 29, in
12 this case the parties agreed that future contributions were trust
13 assets. Therefore, the plaintiffs argue that the failure to pay
14 them when they became due made Eshelman a fiduciary and his
15 failure to pay them was a defalcation. This argument is without
16 merit.

17 14. First, at least as to the unpaid withdrawal liability,
18 assuming one exists, the Ninth Circuit has concluded that a
19 withdrawal liability does not fall within the scope of section
20 523(a)(4) because it arises only after the employer ceases to
21 have an obligation to contribute to the benefit plan. See
22 Carpenters Pension Trust Fund for Northern California v. Moxley
23 (In re Moxley), 734 F.3d 864, 869 (9th Cir. 2013).

24 15. Second, as to the unpaid contributions, assuming there
25 are any, the court conclude that whether or not Eshelman is a
26 fiduciary under ERISA, he is not a fiduciary for purposes of
27 section 523(a)(4). This is because the fiduciary relationship
28 required by section 523(a)(4) must arise before the alleged

1 wrongdoing. See Hemmeter, 242 F.3d at 1190. Put differently,
2 the alleged nondischargeable debt "must arise from a breach of
3 trust obligations imposed by law, separate and distinct from any
4 breach of contract." See In re Baird, 114 B.R. 198, 202 (B.A.P.
5 9th Cir. 1990).

6 16. In this case, the plaintiffs are arguing that Eshelman
7 became a fiduciary when he failed to pay the contributions (and
8 the withdrawal liability), and the failure to pay these debts was
9 a breach of his duty as a fiduciary. However, because the
10 fiduciary obligation arises from the alleged wrongdoing, Eshelman
11 is not a fiduciary under section 523(a)(4).

12 17. Third, assuming this court's conclusions in paragraphs
13 15 and 16 are incorrect by virtue of the language in the trust
14 agreements making future contributions plan assets (see findings
15 in paragraphs 28 and 29 above), the result does not change in
16 this case.¹

17 18. This is because of the Supreme Court's decision in
18 Bullock v. BankChampaign, N.A., 133 S.Ct. 1754 (2013). While
19 this decision was issued after the trial of this matter, the
20 parties had the opportunity to brief its implications in post-
21 trial motions.

22
23 ¹The Ninth Circuit in Moxley discussed an unpublished
24 Eastern District of California District Court case and an out-of-
25 circuit case both determining that a provision in a trust
26 agreement making future benefit contributions plan assets created
27 a fiduciary obligation that existed before the failure to pay
28 those contributions. Hence, these courts concluded that the
failure to pay the contributions amounted to a breach of an
already existing fiduciary duty. Id. at 869. However, because
Moxley did not involve unpaid contributions, only a withdrawal
liability, the Ninth Circuit did not reach the issue.

1 19. In the Ninth Circuit prior to Bullock, "even innocent
2 acts of failure to fully account for money received in trust"
3 were nondischargeable defalcations. See Hemmeter, at 1190.
4 After Bullock, it is not enough to show that a fiduciary has not
5 accounted for or turned over trust assets. In order for this to
6 be a defalcation within the meaning of section 523(a)(4), the
7 plaintiff also must show intentional wrongdoing by the fiduciary.
8 Bullock, at 1759. There is no record of intentional wrongdoing
9 here. See Conclusions of Law at paragraphs 3-6.

10 20. Eshelman believed that because probationary and
11 nonunion employees were not entitled to benefits under the funds,
12 that his company owed no contributions to the funds based on
13 their work. He further believed that his own benefits could be
14 received through his spouse. These beliefs were reasonable and
15 in good faith inasmuch as these practices were disclosed to the
16 plaintiffs, ACSD's records reflecting these practices were made
17 available to plaintiffs' auditors, and at least until 2006 audits
18 made no issue of these practices. In these circumstances, the
19 court cannot conclude that Eshelman understood that additional
20 contributions were owed to the plaintiffs' but nonetheless caused
21 other corporate expenses to be paid while not paying the
22 plaintiffs. Cf. Raso v. Fahey (In re Fahey), 494 B.R. 16 (Bankr.
23 D. Mass. 2013) (concluding that paying corporate expenses to the
24 exclusion of obligations owed to ERISA funds was a breach of the
25 duty of loyalty and a defalcation within the meaning of section
26 523(a)(4)).

27 21. Finally, the plaintiffs' request to reopen the record
28 to address the Bullock issue is without merit inasmuch as the

1 complaint pleaded intentional wrongdoing in the context of claims
2 under section 523(a)(2) and (a)(4). These claims were based on
3 the same nucleus of facts as alleged in context of section
4 523(a)(4). The claim under section 523(a)(2) was dismissed
5 because the alleged fraud was not pleaded with particularity, and
6 the plaintiffs failed to prove the claim under section 523(a)(4)
7 at trial. Nothing was offered suggesting that the defendant's
8 alleged intentional wrongdoing for purposes of section 523(a)(4)
9 was any different than alleged for purposes of sections 523(a)(2)
10 and (a)(6).

11 Accordingly, the motion to reconsider the court's initial
12 decision will be denied. A separate order and judgment shall be
13 lodged by the defendant.

14 Dated: Sept. 9, 2013
15 *March 21, 2015*

By the Court

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17 _____
18 Michael S. McManus, Judge
19 United States Bankruptcy Court
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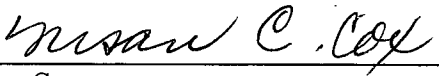
CERTIFICATE OF MAILING

I, Susan C. Cox, in the performance of my duties as a
judicial assistant to the Honorable Michael S. McManus, mailed by
ordinary mail to each of the parties named below a true copy of
the attached document.

Christian L. Raisner
Emily P. Rich
1001 Marina Village Parkway #200
Alameda CA 94501

Wayne A. Silver
333 W El Camino Real #310
Sunnyvale CA 94807

Dated: March 31, 2015



Susan C. Cox
Judicial Assistant to Judge McManus